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Project Report

***BRITISH COLUMBIA FINANCIAL REVIEW:
THE ISSUE OF THE STRUCTURE AND
PROCESS OF FINANCIAL AND POLICY
MANAGEMENT***

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Executive Summary—Structure and Process of Financial and Policy Management

This report evaluates the government's capacity to combine revenue and expenditure decisions with its overall policy goals in the annual budgetary process. The existence of this capacity at the centre of government is essential to support Cabinet policy decisions which impact on deficit reduction.

The current process is inadequate because:

- ▶ There is no coordinated policy development, planning and financial control capacity serving government as a whole.
- ▶ There is no systematic research and analytical support for overall policy formulation.
- ▶ Financial issues tend to be dealt with in isolation.

The report concludes that:

- ▶ The staff support for the Treasury Board Committee of Cabinet must be significantly strengthened, its perspective widened and its role made more strategic.
- ▶ A new staff capacity in support of the Cabinet Planning Board is required.
- ▶ The relationship between the financial and policy planning activities must be coordinated.

To fulfil its enhanced role Treasury Board and its associated economic policy functions should be established as an independent entity headed by a public servant with Deputy Minister status.

There are three different ways in which an enhanced Treasury Board can be combined with a new policy and planning capability. One way is to set up a single, integrated agency that combines budget and planning in one place. A second is to have two agencies, with separate heads reporting to a single public servant. A third is to have two agencies, each reporting to the chairs of their respective Cabinet Committees.

On balance we prefer the first alternative, although the other two could successfully meet the objectives outlined above. However, asking extremely busy Cabinet ministers also to

coordinate the detailed work of two large and complex groups, as in option 3, is probably unwise.

The report also notes the importance of regular program evaluations being the responsibility of the new structure. Evaluations should focus on those major programs through which the bulk of provincial expenditures are made.

This restructuring is essential for planning and achieving deficit reduction in a manner consistent with the government's larger, overall objectives for its term of office.

The Issue of the Structure and Process of Financial and Policy Management

A. Supporting Cabinet committee decision-making

This report examines the capacity of the government's financial decision-making process to undertake long-term, structural deficit reduction, while maintaining a proper balance between financial and non-financial policy objectives.

The only central group regularly supporting decisions on overall government priorities and inter-ministry issues is the Treasury Board staff. However, the present Treasury Board system is primarily concerned with the annual budget preparation and with subsequent expenditure control to ensure compliance with the approved budget. The focus is mostly short-term and tactical rather than long-term and strategic.

Treasury Board, a committee of Cabinet, is supported by a staff of about 35 analysts and directors headed by an assistant deputy minister who reports to the Deputy Minister of Finance and Corporate Relations and the Treasury Board Chair. Analysts are assigned to cover specific ministries and Crown corporations. These staff become quite knowledgeable about the ministries on which they report and are able to advise Treasury Board on financial questions. However, in the case of Crown corporations, we were struck by the limitations on the information available to analysts.

Generally, Treasury Board staff do not have a mandate to raise and aggressively present broad issues to which they believe ministries should respond. Rather, their focus is largely financial and reactive.

Our analysis indicates that in a short-term sense the budget process is being handled adequately, although substantial improvements could be made. This central problem is discussed in our papers on forecasting and financial controls.

The central inadequacy is that:

- ▶ There is no central planning capacity for the government of British Columbia.
- ▶ There is no overall policy development and coordination capacity in support of Cabinet and its committees.
- ▶ There is no systematic research and analysis in support of either overall policy or planning.

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- ▶ Financial issues tend to be dealt with in isolation from policy objectives.

Policy development covers what is to be done and its relative priority; budgeting specifies the appropriate financial resources; and planning integrates the policy and budgetary elements with implementation and delivery choices.

In our view, successful deficit reduction requires the combination of the major policy, budget and planning elements of each major issue to be developed in one place and presented to the right Cabinet committee. Otherwise, one or more of the supports for sound decisions will be missing.

Because of the existing structure, financial choices are apt to appear as incremental or marginal and relatively isolated matters. Each decision is likely to turn on its own immediate merits. It is difficult to form an overview, to appreciate the general trend of events and to see specific choices in relation to the larger flow of affairs.

Seeing each decision as being about unique and distinct matters downplays the cumulative effect of the totality of decisions. Further, there is a tendency to discount the **collective** impact of present choices on the future overall position of the province. There is a significant time discounting of the long-term consequences which minimizes the ultimate true costs. There is a tendency to be excessively optimistic how much costs will increase over time.

There is also a split between expenditure and revenue decisions. The two worlds live somewhat independently. Spending decisions are made all year, but revenue decisions are made at budget time in February.

So it is very possible for spending choices to happen without any clear idea of the full, long-term cost or of how the needed revenue will be raised. This failure to clearly see the full consequences of decisions will continue until:

- ▶ Government policy priorities and deficit reduction goals are clear and well communicated, in enough detail that deputy ministers and Crown CEOs can see what those priorities and goals mean for their entities.
- ▶ The revenue and expenditure choices are **made** to fit these priorities.
- ▶ Means are in place to make certain this actually happens, as approved.

Treasury Board staff has neither the personnel nor the operating mandate to evaluate the actual outcomes of specific programs and delivery systems and offer Cabinet advice on the cost-benefits of optimal allocations of resources. This is unfortunate, because deficit reduction is a long-term exercise that must be done from a broad policy context. It is **not** simply a "cost-cutting" process. Rather it requires a heightened and highly sophisticated

capacity to examine the consequences of various potential allocations of dollars, with the government's core policy values kept firmly in mind. Otherwise, deficit reduction will produce results more negative than necessary and public support will be weakened. But without this support and understanding, deficit reduction goals cannot be reached.

Thus, a new central agency is required to integrate and give equal importance to long-range revenue, expenditure and policy planning and to put these into a framework within which day-to-day spending decisions can be made by ministries.

This agency should be able, as one observer put it "to find the cuts most complementary to where you most want to be".

This will require a comprehensive approach for the full term of office, linking together all the ministries and agencies relevant to particular expenditure issues, reaching out beyond Victoria to the regional operating levels to assess the likely consequences of planned actions.

Finally, the agency must be able to independently evaluate those programs accounting for major annual costs and to identify design changes capable of reducing the rate of cost increases. Evaluations should also assess the comparative performance of programs serving similar objectives, such as economic development and job training programs, so less efficient and effective ones can be phased out.

B. Program evaluation in the B.C. government

Program evaluation is a methodology for assessing the effectiveness of particular programs. It focuses on the following questions:

- ▶ To what extent has the program met its objectives?
- ▶ What impacts occurred as a result of the program?
- ▶ What need is the program addressing, and does that need still exist?
- ▶ Are there more efficient alternatives to the program?

Program evaluation emphasizes impact and effects, not efficiency. For example, it might assess how many new jobs were created as a result of a program. It would not be interested in how many pamphlets were published about the program (except as a factor that might explain effectiveness).

Given the above description of program evaluation, it is safe to say that there is no central policy on the role of or requirements for program evaluation in the ministries, and no comprehensive plan. Program evaluations are done on an ad hoc basis in some

ministries, and not at all in others. For those carrying out evaluations, the following are prevalent problems:

- ▶ The evaluation often starts prior to an appropriate planning phase (sometimes called an evaluation assessment) being done. As a result, key issues are often left out of the evaluation and the programs objectives may be unclear. With no agreement on measuring them, assumptions about existing data are often wrong, and thus inappropriate evaluation methodologies are often used.
- ▶ The clients of the evaluation are often the managers of the programs being evaluated. They draft the Terms of Reference, choose the evaluators, guide the study and approve the final report. They can influence the results and the use which is made of them.

Examples of specific problems reported to us are:

- ▶ Inappropriate measures of effectiveness being used. One program (which gives grants for specific projects to firms in the province) was evaluated using as an indicator of success total sales of the companies involved divided by program funding.
- ▶ Evaluators being chosen for their "agreement to play ball" (quote from one program manager) rather than their objectivity and technical ability.
- ▶ We see an almost total focus on gross impacts rather than what are sometimes called incremental impacts, that is, those that would not have occurred without the program. For example, suppose a program's major objective was to stimulate a certain kind of R&D in the province, and this was accomplished via grants to specific firms. One could measure the R&D carried out in total by the program participants. We would call this a gross impact, and it would be a relatively large number (and therefore, from a program manager's perspective, a nice one to measure and report). However, some or all of the R&D might have occurred without the program. It is obviously harder to measure incremental impacts, but unless some attempt is made, the evaluation results are largely meaningless. Very little effort in the B.C. government is expended toward assessing true program effectiveness.

In summary, program evaluation is an extremely important part of better financial management and the key function for choosing among programs or for changes to funding. But there is little evaluation information available. What exists is generally unreliable or of little value for making dollar allocation decisions. It is up to the government, via a central agency, to establish appropriate evaluation guidelines, including who is the client of the evaluation, who carries it out, the drafting of valid and appropriate Terms of Reference, and review processes that result in valid and unbiased conclusions.

What structure can serve these objectives?

C. The conceptual alternatives

No perfect working model exists of the required agency. Consideration of various structures and processes must be the starting point. A **tailored approach** is required, so that the solution is appropriate for this environment.

There are two possible models:

- ▶ Create a new policy and planning group supporting decision-making by Cabinet's planning committee(s) and integrate it with an expanded and enhanced group for revenue and expenditure planning using the current Treasury Board staff as the foundation.
- ▶ Keep policy planning and financial control as separate but linked agencies.

Within these two models, obviously, there are many sub-alternatives related to roles, responsibilities, structures, and staffing levels. However, it appears that there are strong philosophical and practical advantages to separating the existing Treasury Board staff from the Finance Ministry and linking it with a new planning agency:

- ▶ Both symbolically and practically, the long-term policy perspectives and the short-term expenditure management support activities would be together.
- ▶ Using the existing base would allow a quick start up, with a core staff already in place.
- ▶ This would allow for the full utilization of Treasury Board staff's knowledge and experience, and integration of those into a common longer-term policy framework for this government.

1. The key components

A number of important elements must be defined. Two of the most important are the **founding principles**, and the **characteristics of the process**.

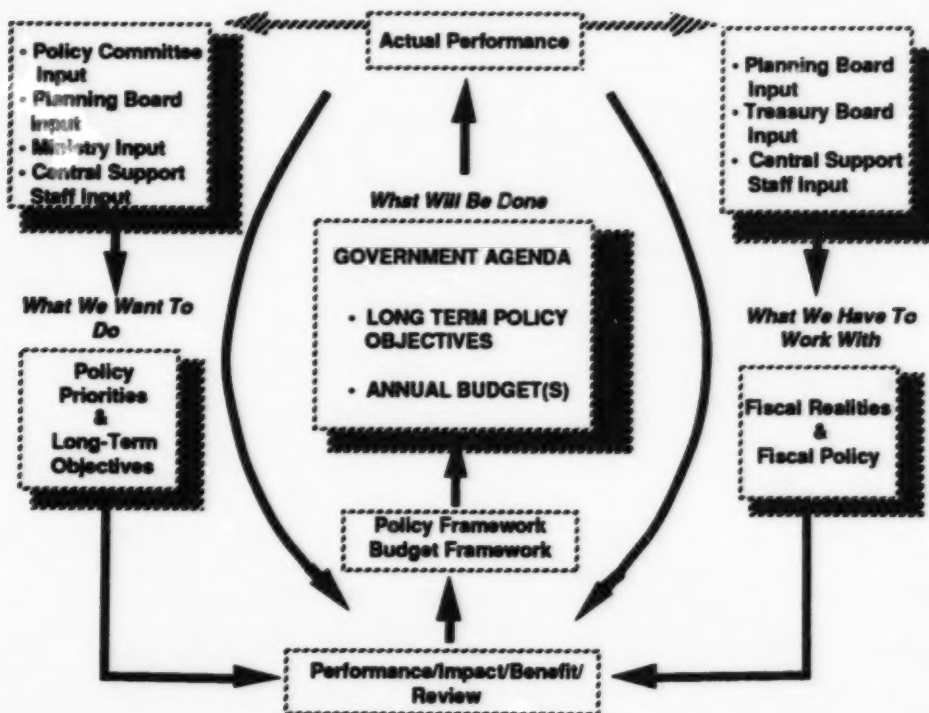
2. Principles

Given the experience from other jurisdictions, a number of principles are central to the success of a model supporting Cabinet committee decision-making:

- ▶ **Linkage of revenue and expenditure planning, management, and decision-making.** In other words, alignment of the responsibility for spending with the responsibility for raising taxes.
- ▶ **Linkage of longer-term policies and priorities with shorter-term management and control decisions.**

- ▶ **A government-wide perspective** on day-to-day operational decision-making.
- ▶ Regarding the **government's policy agenda** as the major driving force for expenditure and program decisions.
- ▶ **One-stop-shopping** for those who need decisions to be made, notably in the ministries, and particularly for expenditure-related and new policy decisions.
- ▶ **Early and effective management of conflict** without stifling the essential competition among ideas and competition for resources.
- ▶ **Continual linkage between macro and micro policy issues.**

Exhibit
Integration objectives for budgeting



3. Process

The decision-making process must be carefully designed and managed to balance conflicting influences on decisions, and to avoid an excessive central government role. The staff support to decision-makers must include three components:

- ▶ A reactive role, reviewing material submitted by ministries.
- ▶ A directive and development role, performing cross-ministry analysis of issues, policies, programs and impacts, joint studies with ministries on priority policy matters, and providing cross-jurisdictional comparative information where appropriate.
- ▶ An overall (re)orientation to a benefit/impact and outcome framework for discussion and decision-making. This means placing more emphasis on the comparative public benefits of the competing potential outcomes of scarce dollars.

It will be very difficult to prevent the first role from crowding out the latter two, given the ease of reacting as opposed to initiating, and also considering the potential for the ministry-originated workload to drive the agenda with input-related requests. The financial side will tend to be short-term, the policy side long-term, so joining them will help to provide balance.

4. Structure

As to the structure itself, on balance, we believe the task requires the coordination of Treasury Board staff with a new planning secretariat. It would use the existing Economic and Policy Division, Planning and Statistics Division and Treasury Board staff of the Ministry of Finance and Corporate Relations as the base; and it would add to this additional policy and planning staff. These Divisions already have about 120 staff. Added to this should be 25 or so analysts able to carry out the non-financial dimensions of the task.

There are three ways in which coordination could occur. A single agency could be formed and headed by a single deputy minister. This person could report either to the chair of the Cabinet Planning Board or to the Chair of Treasury Board, with the other chair consulted on all relevant matters. Secondly, separate Treasury and Planning agencies each could be headed by a deputy minister. Finally, the finance agency head would report to Treasury Board chair, and the planning agency head to the Planning Board chair. In the latter two cases, coordination could occur between the two chairs or through the office of the Premier's deputy minister.

The linked or combined agency should have divisions devoted to:

- ▶ Fiscal and budget analysis (the core of the "old" Treasury Board staff functions). This would include: tax, fiscal and economic policy, and budget legislation and estimates.
- ▶ Social policy, covering health, social services, education and justice. This can be based on the social policy segment of Treasury Board staff.
- ▶ Economics and labour (this is primarily existing in the Economics and Policy Division) looking after economic development, labour and natural resources.
- ▶ Environment—We have noted elsewhere our view that the environment and the costs associated with its use are of strategic value in expenditure planning and management. This group could be extended to handle land use and transportation policy as well. At the moment neither is being properly coordinated with a view to linking relevant ministries and finding inter-ministerial solutions to problems that require new policy.

Main functions should be:

- ▶ Support to the Cabinet's Planning Board and Treasury Board committees, by assessing all submissions.
- ▶ Linking financial planning and policy development.
- ▶ Control of the annual budget preparation.
- ▶ Development and enforcement, once approved by Cabinet, of a fiscal framework and all related plans including the deficit reduction plan.
- ▶ Develop and conduct evaluations of major ministerial programs, as part of its long-term assessment of outputs and outcomes.
- ▶ Coordination of ministry planning exercises in a government-wide framework.
- ▶ Facilitation of inter-ministerial cooperation.
- ▶ Development of a planning framework.
- ▶ Support to and learn with other Cabinet committees as required.
- ▶ Relationship with the Crown Secretariat.

D. The next step—Important considerations

Key considerations in moving to implement the preferred conceptual alternative include:

- ▶ Definition of the **organizational model**.
- ▶ Definition of **roles and responsibilities** in relation to Cabinet for the committees and their staff.
- ▶ Definition of the committee **process**, particularly the balance of time devoted to the short-term and long-term perspectives.
- ▶ **Communication** of the new process and expectations to all ministries and deputies.
- ▶ **Staffing**.

Initial focus will necessarily be on these questions:

- ▶ To what extent, if any, will the committee staff be expected to undertake **policy development** as opposed to **challenging policy proposals** that come forward from ministries (i.e., initiated by the ministry or by a directive from the centre?)
- ▶ To what extent should the **division of roles and responsibilities** mirror the traditional "hard side/soft side", "economic development/social resources" frameworks?
- ▶ What **cornerstone activities** can be established to focus routine attention on longer-term policy objectives (i.e., as the budgeting process focuses on the shorter term)?
- ▶ How should the current Treasury Board support functions be incorporated into the new Committee Support structure? In particular, how should the tax policy and federal-provincial relations components be dealt with?
- ▶ Should the Planning and Treasury Boards become one board for some or all discussion and decision-making requirements?
- ▶ How can a long-term expenditure reduction focus become a driving force in the operation of the Planning and Treasury Board functions?
- ▶ What are the key policy issues?
- ▶ How can the annual budget, as the essence of the government's annual management plan and policy delivery mechanism, be (re)oriented towards fulfilling the long-term and policy agenda of the government?

There is one large risk that must be frankly acknowledged and provided for in advance, so that it does not become a problem. This concerns the relationship of the new planning secretariat with line ministries and their senior executives.

There is some chance that this new structure could complicate rather than expedite already cumbersome approval processes. As one deputy minister put it: "no one can do anything cleanly anymore". By this, he meant that the procedure for getting approvals for any important action is so uncertain and changeable as often to make constructive action impossible. It is in the interest of everyone that deputy ministers have a clear and unambiguous pathway for securing approvals of major decisions. It is also essential that ministers and deputies not lose the capacity to plan for and direct the affairs of their ministries.

The division of authority between the central agency and the ministries is one of two vital relationship issues. In principle, this central agency might be responsible for setting the framework for ministerial plans, making sure they are completed on time, supporting Cabinet decisions and then monitoring the results.

It must also be able to identify and initiate special projects that serve key policy objectives. Ministry decision requests must be facilitated. Ministries must also be given a clear sense of overall direction of their general role in achieving this. If this central agency in fact contributes a coherent sense of common purpose and actively helps ministries to achieve their part in this larger enterprise, it will receive cooperation. To that end, an advisory committee of selected deputy ministers should be considered.

E. Recommendation

A single policy and planning agency would be more powerful, but also arouse more concern by deputy ministers and be potentially more of a bottle-neck. It could offer more internal integration of competing interests. Two distinct agencies would arouse fewer fears and less resistance but would have the potential for sharp inter-agency conflicts and would be less able to initiate cross-ministry reviews and consistent, government-wide action. On balance, and while acknowledging the risks, we prefer the single agency, feeling it more likely to have the stronger capacity appropriate to the size of the deficit.